BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

Order Instituting Rulemaking to Implement the Commission's Procurement Incentive Framework and to Examine the Integration of Greenhouse Gas Emissions Standards into Procurement Policies.	)	**Rulemaking 06-04-009 (Filed April 13, 2006)**
In the Matter of:	)	**CEC**
	)	**Docket 07-OIIP-01**
AB 32 Implementation: Greenhouse Gases.	)	

PREHEARING CONFERENCE STATEMENT OF THE AMERICAN GAS ASSOCIATION

Paul Wilkinson
Vice President-Policy Analysis
American Gas Association
400 North Capitol Street, NW
Washington, DC 20001
(202) 824-7125
(202) 824-9135
Pwilkinson@aga.org

Pamela A. Lacey
Senior Managing Counsel
American Gas Association
400 North Capitol St. N.W.
Washington, D.C. 20003
(202) 824-7340
(202) 824-7082 - fax
placey@aga.org

Dated: July 26, 2007

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On the Preliminary Recommendations of the California Public Utilities Commission Staff for the Treatment of Natural Gas Sector Greenhouse Gas Emissions

July 26, 2007

Pursuant to the July 12, 2007 **RULING OF THE ASSIGNED ADMINISTRATIVE LAW JUDGES REGARDING COMMENTS ON STAFF NATURAL GAS PROPOSAL AND NOTICE OF PREHEARING CONFERENCE** (Ruling), the American Gas Association respectfully submits this Prehearing Conference Statement.

I. Introduction

The American Gas Association (AGA) represents 200 local energy utility companies that deliver natural gas throughout the United States. Our members provide natural gas service to 64 million homes, businesses and industrial facilities and 92 percent of all natural gas that is distributed by local utility companies in this country is distributed by AGA members. In addition, virtually all natural gas distributed in the state of California is provided by AGA member companies. We are very pleased to provide comments to the California Public Utilities Commission on this issue of critical national and global importance.

Given its important historical leadership on environmental issues, it is clear that a greenhouse gas reduction program implemented in California will have an impact on the construction of other state, regional and national programs. We therefore believe that it is important for AGA to comment on the CPUC recommendations. We note, however, that some conditions in California, such as the mix of electricity generation sources, differ from conditions in other states. Therefore, some of our comments may be more applicable in other states or at the national level than in California. Nevertheless, we include these comments for consideration.

II. AGA and its members support the need to reduce greenhouse gas emissions.

A task force of AGA member company chief executives was formed in 2005 to address the issue of climate change. Although the association had developed climate change principles nearly a decade earlier, it was determined that our position should be reevaluated in light of advances in the science of climate change as well as changes in public policy and public opinion. As a result of this reevaluation, a new set of climate change principles was adopted by the AGA Board of Directors on February 19, 2007 (copy attached).

The AGA principles note that reducing greenhouse gas emissions can provide multiple national benefits in addition to environmental benefits, including reducing oil imports and diversifying our electricity generating mix. The principles state that all sectors of the economy should contribute to reducing greenhouse gas emissions, but that a uniform approach for all sectors might not be desirable. That is, an understanding of the contribution of that sector to overall greenhouse gas emissions, and how emissions are generated within that sector should be considered in order to establish the most cost-effective, equitable and efficient reduction program for that sector. This point is particularly germane to the CPUC recommendations.

III. Natural gas utilities and their customers should play a significant role in any greenhouse gas reduction program.

Natural gas is a premiere fuel from an environmental perspective. It emits very low levels of most pollutants relative to other fuels. In addition, natural gas is very efficient in its production, transportation and use. That is, when natural gas is used, very little fuel is wasted from the point of production through consumption. This combination of relatively low pollutant levels and high efficiency levels results in less impact than other fossil fuels with respect to most environmental issues – including climate change, acid rain, urban smog, solid waste, water quality and visibility. This combination of attributes is particularly noteworthy with respect to climate change in that it reflects the two fundamental keys to reducing greenhouse gas emissions - use cleaner fuels and use them as efficiently as possible.

The use of natural gas in high efficiency residential, commercial and industrial applications is key to any attempt to lower U.S. greenhouse gas emissions. From residential water heaters to industrial furnaces and combined heat and power systems, natural gas can provide benefits. Natural gas can also be used to generate electricity. Gas-fired electric generation is increasing nationally, and supplies at reasonable prices must be made available to facilitate its growth. Since domestic supplies are forecast to remain flat over the short to medium term and decline in the long term, new supply sources, such as imported liquefied natural gas (LNG), are needed to fill the expected gap between supply and demand for natural gas. In addition to natural gas available from many new and existing sources, the use of other means of generating electricity cleanly should be promoted – including nuclear, IGCC, wind, solar and other renewable energy forms.

IV. The differences between natural gas and electric utilities should be recognized in any greenhouse gas reduction program.

- **Natural gas consumption (and associated greenhouse gas emissions) has grown much more modestly than electricity consumption**. The stated goal of the California Global Warming Solutions Act of 2006 is to reduce greenhouse gas emissions to 1990 levels by 2020. In contrast to other emission sources, natural gas consumption and related greenhouse gas emissions for non-electricity applications have shown very little growth or even declined since 1990. On a national basis, residential natural gas consumption in 2006 was lower than in 1990 and lower than in any year since 1990. Residential and commercial consumption combined were only approximately 2.9 percent higher in 2006 than in 1990. (See: U.S. Energy Information Administration web site.) For the state of California, combined residential/commercial gas consumption was 5 percent lower in 2004 than in 1990. (Data provided by the U. S. Energy Information Administration, *State Energy Consumption, Price and Expenditures Estimates*, June 2007 update; 2004 is the most recent state data available.)

- **Natural gas utilities do not have the same opportunities as electric utilities to control greenhouse gas emissions.** Electric utilities can meet carbon reduction targets either by promoting conservation and efficiency by end-use customers or by the substitution of low-carbon generation options (such as solar, wind, nuclear, and carbon capture and storage). Gas utilities can also promote conservation and efficiency, but they have virtually no ability to substitute low carbon alternatives to natural gas. (There may be some very limited potential through bio gas, landfill methane, or other substitutes.)

- **Natural gas utilities have been very supportive of innovative rate designs which have enhanced their ability to actively promote conservation and efficiency.** Traditional rate design structures often made it difficult for natural gas utilities to aggressively promote natural gas conservation and efficiency by their customers.

To do so could have had negative financial consequences as a result of lower volumes of natural gas transported and sold. California has been a leader in breaking the link between a utility's earnings and energy consumption, having adopted – and maintained – "decoupled" rates for many years. Today, in an effort to more closely align the interests of the consumer and the gas utility with environmental/energy efficiency objectives, a number of states, including California, have moved away from the traditional rate structure to revenue decoupling or other non-volumetric rate designs such as weather normalization, rate stabilization or some form of a flat monthly fee. Currently, 29 states have adopted some form of non-volumetric rate structure, including 11 that have adopted revenue decoupling. In addition, 10 states currently have non-volumetric rate programs pending, including 8 states that are considering revenue decoupling. We believe the adoption of these innovative rate designs has had a significant impact on the ability of gas utilities to promote conservation and efficiency and we believe the stable or declining natural gas consumption levels experienced since 1990 are in part attributable to this promotion.

- **Conservation and efficiency programs can be continued, expanded and/or coupled with new appliance standards and building shell standards to further reduce greenhouse gas emissions.** We believe that these programs have been effective and that further progress is achievable. It is not clear that a cap and trade program in this sector would be more environmentally effective, nor is it clear that such a program would be cost effective or that it would operate smoothly for natural gas utilities. For example, the CPUC already has an aggressive performance-based natural gas efficiency program. That should be further investigated to determine its applicability to the AB 32 targets.

V. Using natural gas directly in residential, commercial and high efficiency industrial applications can be the most efficient and carbon-effective way to utilize gas.

Energy is used or lost at various points in the energy chain – energy production, transmission, distribution, conversion to electricity, etc. Thus, residential energy consumption can produce greenhouse gases at the residence, but it also can result in emissions at various points along the chain, from the energy consumption required to run natural gas transmission compressors to the boilers or turbines used to generate electricity. Minimizing energy used or lost along the energy chain minimizes greenhouse gas emissions. When natural gas is used directly in residential, commercial and high efficiency industrial application, it is used very efficiently – only about 10 percent of the energy produced is used or lost as it moves from the point of production to the consumer. In contrast, about 70 percent is lost if the natural gas is converted to electricity in a traditional boiler/steam turbine operation. The loss would be less if the electricity were produced via higher efficiency combined cycle plants, but still in the 45 percent range. (See: *Public Policy and Real Energy Efficiency*, prepared by GARD Analytics for the American Gas Foundation, October 2005, page iii.) For example, when all energy used or lost is considered, including the energy used by the residential appliance, a natural gas water heater results in about one-third to one-half the CO_2 emissions of an electric resistance water heater.

- **A poorly designed greenhouse gas reduction program could push customers away from natural gas in favor of electricity with negative carbon consequences.** The CPUC draft notes that a hard cap for electric utilities but no cap for natural gas utilities could result in some shifting to natural gas. We believe that if some such shifting did occur it could be a good thing from a greenhouse gas emission perspective and from a practical perspective. As noted above, we believe that using natural gas directly is the most efficient and effective form of use. In fact, however, a more likely result of the CPUC recommendations might be the switching of residential and commercial customers from natural gas to electricity. In a cap and

trade system where natural gas utilities have very little ability to produce surplus allowances, in contrast to electric utilities that have the ability to switch their generation mode, we believe that counter-productive gas-to-electric shifting is quite possible. (Altering the generating mode may be less of an option for electric utilities in California due to a lower reliance on coal-based generation for most electric utilities in the state relative to utilities in other parts of the country.) Such shifting would ultimately force the construction of more generating plants when low-carbon emitting generating options are certain to be scarce.

- **Using natural gas in direct residential, commercial and high efficiency industrial applications could reduce the need to construct new electricity generating plants.** Electric utilities are facing very dramatic emission reduction targets and many of the compliance options they are expected to use face serious regulatory, economic and technologic hurdles – from wind and solar power to carbon capture and sequestration technologies to nuclear power. Switching load to residential and commercial natural gas customers may provide an alternative to the construction of new generating plants. This alternative could be particularly important over the next several decades as low carbon generating technologies are in the developmental stage.

VI. Greenhouse gas emissions attributable to gas utility operations are very modest and utilities have voluntarily been involved in the EPA Star program to ensure that such emissions are minimized.

Many AGA member companies voluntarily participate in programs to report and/or reduce greenhouse gas emissions. The U.S. Environmental Protection Agency (EPA) has an innovative program called Natural Gas STAR that is a voluntary partnership between EPA and industry to reduce methane emissions from the natural gas system cost-effectively. AGA has been an official endorser and supporter of the EPA Natural Gas STAR program since 1993. The program helps facilitate technology and idea sharing, so

that participants can develop best practices for methane reduction projects. Forty-seven AGA member companies participate. Through 2005, these gas utility companies have implemented STAR projects that have reduced emissions from their transmission, storage and distribution facilities by nearly 46 billion cubic feet.

To put the STAR reductions in perspective, the DOE Energy Information Administration (EIA) reports that in 2005, the U.S. natural gas production, processing, transmission, storage, and distribution segments emitted methane with a CO_2 equivalence of 154.7 million metric tons. (See: U.S. EIA, *Emissions of Greenhouse Gases in the United States, 2005*, p.40.) Of this total, natural gas distribution accounted for 42.6 million metric tons. EIA reports that Natural Gas STAR methane reductions for all 5 natural gas segments totaled 34.7 million metric tons in CO_2 equivalence. Many gas utilities are also involved in projects to voluntarily report greenhouse gas emissions to the U.S. Department of Energy (DOE) and/or the California Climate Action Registry (CCAR).

AGA appreciates the opportunity to comment and to participate in this proceeding. We look forward to working with the Commission and other parties regarding greenhouse gas policies that will affect our natural gas utility members.

Dated this 26th day of July, 2007 at Washington, D.C.

Respectfully submitted,

Paul Wilkinson
Vice President-Policy Analysis
American Gas Association
400 North Capitol Street, NW
Washington, DC 20001
(202) 824-7125
(202) 824-9135 - fax
Pwilkinson@aga.org

ATTACHMENT

AGA Climate Change Principles

February 19, 2007

Introduction

Natural gas is a premiere fuel from an environmental perspective. It contains very low levels of most pollutants relative to other fuels. In addition, natural gas is very efficient in its production, transportation and use. That is, when natural gas is used, very little fuel is wasted from the point of production through consumption. This combination of relatively low pollutant levels and high efficiency levels results in less impact than other fuels with respect to most environmental issues – including climate change, acid rain, urban smog, solid waste, water quality and visibility. This combination of attributes is particularly noteworthy with respect to climate change in that it represents the two fundamental keys to reducing greenhouse gas emissions - use clean fuels and use them efficiently.

The use of natural gas in high efficiency residential, commercial and industrial applications is key to any attempt to lower U.S. greenhouse gas emissions. From residential water heaters to industrial furnaces and combined heat and power systems, natural gas can provide benefits. Natural gas can also be used to generate electricity. However, there has been an over-reliance on natural gas for new electricity generators over the past 10 to 15 years, particularly in light of ongoing restrictions to natural gas supplies. Therefore, the use of other means of generating electricity cleanly should be promoted – including nuclear, IGCC, wind, solar and other renewables.

Although natural gas should be a cornerstone in any viable greenhouse gas reduction program, restrictions on access to natural gas supplies and on the infrastructure necessary to produce, transport and import natural gas limit the use of this fuel for environmental gain. In addition, these restrictions have resulted in higher and more volatile natural gas prices, pushing some consumers to less environmentally attractive competing energy forms. The potential for natural gas to contribute from an environmental perspective cannot be realized unless access to the resource is increased.

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The following Principles elaborate on how natural gas can most effectively be used to reduce greenhouse gas emissions while protecting the interests of homeowners, small businesses and manufacturers.

1. **Based on a growing understanding of the science of climate change, reasonable and responsible federal action to reduce greenhouse gas emissions is warranted. Such action must be developed in concert with national energy and economic conditions and goals.**
    - The causes and potential effects of climate change are complex, and total agreement on these issues is highly unlikely. Scientific and public opinion have become more definitive over time and together suggest we have reached a tipping point on the issue – we should fully expect political action to follow.

- The principal means of reducing greenhouse gas emissions and the potential for climate change is to use cleaner energy sources and to more efficiently utilize all forms of energy. These actions should be promoted in that they can provide multiple national benefits, from lowering consumer energy bills to reducing oil imports and diversifying our electricity generating mix.

- Reducing greenhouse gas emissions can be very costly, and any control program implemented should include a comprehensive evaluation of all associated costs and benefits – from the point of energy production through energy consumption.

- AGA will evaluate climate change proposals to determine their impact on natural gas utilities, energy markets and our customers.

2. All sectors of the economy should contribute to reducing greenhouse gas emissions and any control program should seek to maximize efficiency and effectiveness while minimizing overall costs. Each sector should be dealt with in a manner consistent with its economic impact, its contribution to the problem and the degree to which it can help reduce greenhouse gas emissions; therefore a uniform program for all sectors may not be desirable.

- Greenhouse gases are emitted throughout all sectors of the economy and reductions are achievable in all sectors. However, it is clear that emissions are fairly concentrated and that some sectors account for a relatively small percentage of total overall emissions. For example, residential natural gas users account for only about 5 percent of total U.S. fossil-fuel CO_2 emissions. An effective climate change program must recognize the differences in sectoral contributions and in potential sectoral reduction strategies. For example in the transportation sector, revised CAFÉ standards might be more effective than a gasoline tax.

- Natural gas utilities, in addition to reducing their own operational emissions, can assist their customers in reducing emissions by providing a variety of services, information and programs and by supporting strong but reasonable building

and appliance efficiency codes and standards. Further, a number of gas utilities have worked with their state regulators to develop rate structures that allow them to promote efficiency by their customers without causing financial hardship to the utility.

3. High efficiency end-use natural gas applications should be a cornerstone of any greenhouse gas emission reduction program.

- In addition to containing significantly lower levels of greenhouse gases than other fuels, natural gas is also very efficient to transport and use. Thus, using natural gas in place of other fuels can provide energy to consumers while reducing emissions. When a complete environmental assessment is made, including consideration of all emissions from the point of production through consumption, natural gas is particularly attractive. For example, using gas-fired residential water heaters ultimately results in about one-third the CO_2 emissions of electric water heaters.

- The use of natural gas for traditional applications with high efficiency equipment can significantly reduce greenhouse gas emissions relative to equipment fueled by other energy forms or by older natural gas equipment. In addition, new natural gas-based applications, such as combined heat and power systems, fuel cells and natural gas vehicles offer similar benefits.

4. A diverse mix of low greenhouse gas emitting energy sources – including solar, wind and other renewables, clean coal and nuclear power – should be promoted for both new and existing large-scale electricity generation facilities.

- Natural gas can be used to generate electricity in both small- and large-scale applications with high efficiency and relatively low emissions of CO_2.

- However, partly attributable to its environmental performance, natural gas has become almost the sole source of new electricity generating capacity in the U.S. The demand growth in gas-fired electricity generation, in conjunction with severe constraints to increasing natural gas supplies, is a significant factor in the dramatic increase in natural gas prices since 2000.

- Other low CO_2-emitting forms of electricity generation should be promoted in order to reduce emissions without further exacerbating the reliance on natural gas.

5. Natural gas prices have risen significantly in recent years, and climate change mitigation actions should be carefully constructed so that the potential benefits of natural gas are not impeded.

- The price of natural gas has risen dramatically over the past 6 years. For example, residential natural gas prices are up roughly 60 percent since 2000. These high prices have strained consumers, particularly low income consumers, while also contributing to industrial plant shutdowns and unemployment.

- Residential consumers have reduced their consumption of natural gas by 25 percent per household since 1980, largely attributable to tighter homes and more efficient appliances. Any climate change mitigation actions should be carefully structured so that they do not have the unintended consequence of diverting energy consumers from natural gas to less efficient and more polluting competing energy forms.

- Natural gas utilities can effectively help reduce greenhouse gas emissions through programs aimed at increasing customer awareness of energy efficient technologies and practices, rate structures that promote efficiency, support of codes and standards that promote efficient homes and appliances, and other measures developed by natural gas utilities in concert with their customers and public utility commissions.

6. Any emission reduction program should focus on energy consumers and/or producers, not on local distribution companies.

- How much energy is used in our economy is determined fundamentally by the producers and consumers of that energy. Producers decide how much to produce at various market price levels, and consumers decide how much to consume and how and when to invest in energy consuming equipment of various efficiency capabilities. Because producers and consumers make these fundamental decisions, any climate change program must focus on them – in terms of procuring allowances, reporting requirements, etc.

- Local natural gas utilities merely transport energy; they do not make the fundamental decisions about energy consumption levels and equipment purchases.

- Local natural gas utilities do consume a small amount of energy in the equipment used to transport and store gas and some very minor volumes of natural gas may also leak at various points in their system. The energy that is used or lost by the local utility is generally 1 percent or less of their total throughput, and gas utilities have been working with the Environmental Protection Agency and others to research, develop and deploy new technologies that minimize system leakage. In any climate change program, local natural gas utilities should be responsible for the energy actually used or lost in their daily operations.

7. In order for natural gas to fully contribute in terms of reducing greenhouse gas emissions, natural gas supplies must be increased.

- The wise use of natural gas can help ease a number of environmental problems – including climate change, acid rain, urban smog, visibility and water quality issues.

- However, drilling for natural gas is prohibited off the East Coast of the U.S., the West Coast, the eastern Gulf of Mexico and much of the Intermountain West. Public policy must allow greater access to natural gas in these areas. Additionally, attempts to increase natural gas supply infrastructure, from LNG receiving terminals to underground pipelines and storage facilities, should be promoted by national energy policy. Consistent with this policy direction, increased access to natural gas resources and the development of requisite infrastructure should proceed in a manner that ensures careful siting and operation of production and delivery facilities.

- The demand for natural gas is likely to increase by 20 to 30 percent over the next 15 years based on both economic growth and environmental grounds. Meeting national goals - both environmental and economic – will require greater access to domestic and international gas supplies.

Certificate of Service

I certify that, pursuant to the Commission's Rules of Practice and Procedure, I have this day, by mail, or by electronic mail to the parties for which an electronic mail address has been provided, served a true copy of the Prehearing Conference Statement of the American Gas Association on all parties identified on the attached service list for R.06-04-009.

Executed this 26th day of July, 2007, at Washington, D.C.

Senior Managing Counsel
American Gas Association
400 North Capitol St. N.W.
Washington, D.C. 20003
(202) 824-7340
(202) 824-7082 - fax
placey@aga.org